FIDC

Finance Industry Development Council

(A body incorporated as a Self Regulatory Organisation for Registered NBFCs)

1 October 2008

Dr. D Subbarao
Governor
Reserve Bank of India
Central Office Bldg, 18th Floor
Shahid Bhagat Singh Road
Mumbai 400 001.

Respected Sir,

At the outset, we place on record our sincere thanks for giving us the opportunity to present our views on the key issues affecting NBFC-AFCs. We wish to place before you the following points for your kind and favourable consideration:

1.Capital adequacy:

RBI vide it circular No.RBI/2008-09/116 (DNBS (PD).CC.No.125/03.05.2002/ 2008-2009 dated 1st August 2008 has stipulated that NBFCs-ND-SI should increase the minimum Capital to Risk-Assets Ratio (CRAR) from the present 10% to 12% by March 31, 2009 and further to 15% by March 2010.

While the move to raise it from 10% to 12% is in keeping with the current regulatory environment, raising it further to 15% for NBFCs-ND-SI would be unduly harsh. It has been our consistent and longstanding submission to RBI that capital allocation should ultimately reflect the appropriate level of risk inherent in the assets financed by NBFCs. Under the present dispensation, all the assets financed by NBFCs, regardless of whether they are secured or unsecured and regardless of the risks associated with different classes of assets, carry a uniform risk weightage of 100%. It is a well documented fact, based on detailed analysis undertaken by credit rating agencies that commercial vehicles, cars and construction equipment have a much lower risk profile, as compared to

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other categories of assets. These assets, by their very nature, are easily saleable and realise significant residual values and therefore deserve to be treated on a different footing from other assets. Needless, to add, unsecured loans fall in a different risk category altogether. In light of the above, the risk weightage for assets financed by NBFCs should be suitably revised to reflect the varying risk profiles, as follows:

- Commercial Vehicles, Cars & Multi utility vehicles – 50%
- Construction & Material handling Equipment & Tractors – 50%
- Loans against Gold and Silver ornaments upto to Rs.1 lakh – 50%
- Three Wheelers – 75%
- Two Wheelers and Industrial Equipment – 100%

It is our submission that this would duly reflect the appropriate levels of risk inherent in the respective asset classes and provide NBFC-AFCs a degree of capital relief. This is also in consonance with the Basel II framework for Banks.

2.Long Term Funding:

Sir, We have over the years, put forth our case for stable long term funding for NBFC-AFCs. Given the nature of our business and the type of assets financed by us, tenors typically tend to be between 36-60 months. With banks often being reluctant to fund NBFC-AFCs, there is an urgent need for an alternative source of long term funding. Thanks to the initiatives taken by Reserve Bank of India, SIDBI has recently started to entertain funding proposals from NBFCs. Given the fact that a reasonable proportion of our advances go directly or indirectly to the agricultural sector, it would be a great support, if NABARD can also extend long term loans to NBFC-AFCs.

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Given the limitations of medium term funding from domestic sources, there is a strong case to allow NBFC-AFCs to access External Commercial Borrowings (ECB). This would enable them to access medium to long term funds from the global financial markets and channalise them into financing of infrastructure projects and productive assets, which in turn aid in capital formation. Needless to state, appropriate conditions may be stipulated for the raising of ECBs.

3.Repossession Guidelines:

The issue of repossession has assumed alarming proportions, with a plethora of judicial and quasi-judicial pronouncements on the subject. Whereas, asset financing NBFCs resort to the appointment of "Repossession Agents" to secure the specific asset financed by them, Lenders, who give out unsecured loans engage "Recovery Agents" who tend in many instances, to take away any asset that is available with the defaulting borrower. We strongly believe that a distinction needs to be drawn between repossession agents and recovery agents and the guidelines governing these two need to be distinct.

4.Taxation Issues:

Sir, as presented to you, we have represented, unsuccessfully, over many years to the Ministry of Finance in matters related to income recognition and provision for bad and doubtful debts under the RBI prudential norms. While banks and housing finance companies are afforded the tax set offs in respect of these, NBFCs alone have been singled out for a discriminatory treatment. We seek your good offices in prevailing upon the Ministry of Finance to bring parity amongst the constituents of the financial sector.

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Sir, we are extremely grateful to you for your appreciation of the issues concerning NBFCs and the timely support and guidance that we have received all along from RBI. We are confident that the above submissions too, will receive your favourable consideration in order that NBFC-AFCs may continue to play an important role in the economic growth of our country.

Thanking you once again.

With regards,

Sincerely,

T.T.Srinivasaraghavan
Chairman

Copy to :

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